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THE SECRETARY OF STATE
WASHINGTON 25, D. C.

DEPARTMENT OF STATE

WASHINGTON



51173

June 1, 1950

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To: The Central Intelligence Agency
Office of Reports and Estimates

From: The Department of State
Office of Intelligence Research

Subject: 24-50, "French Prospects in 1952/53".

Attached herewith are two copies of OIR documents

French Viability in 1952/53, and

Notes on French Agricultural Prospects,
1952/53.

The French viability paper summarizes the OIR positions on French prospects for viability in 1952/53. The notes on agriculture gives substantiating details on agriculture.

Notes on financial stability and industrial production, giving further substantiating details, will follow Friday, June 2, and the following Monday.

Allan Evans,
Director
Office of Intelligence Research

Enclosure:

2 copies of 24-100 "French
Prospects in 1952/53"

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FRANCE: NOTES ON VIABILITY AND THE DOLLAR GAP

The French economy will be "viable" if it can provide an increasing standard of living for its people without the necessity for extraordinary foreign assistance. There is every reason to believe that after the end of the Marshall Plan this will be the case. The hardcore of a dollar deficit, which now seems likely to remain, is one which is "manageable". A summary of the reasoning on which this conclusion is based is given in the following notes.

A "viable" France by 1952/53 will be possible only in a peaceful world and probably only in a world where international and national tensions are at least not significantly greater than they are today. An increase in tension would by itself have unfavorable economic repercussions in France. If a greatly increased military burden were added, the economy could not bear it without foreign assistance. This paper assumes that if a large increase in French military forces is required, part of its financial cost will be defrayed by the U.S. It is also assumed that other nations continue to expand their income and increase their foreign trade along with France.

Increasing Domestic Production

The main pillar of France's standard of living is obviously the production of its people. The French standard of living has risen since the war largely because French production has risen. With current full employment, further increases in production depend upon increasing the productivity of each French laborer.

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Output per worker in France has increased sharply during the past year and is now at levels at least equal to those prevailing in the best prewar year. This rather striking increase is less encouraging than it might seem. It reflects essentially the breaking of most of the postwar bottlenecks. It does not necessarily indicate the beginning of an upward trend which may be expected to carry output to new high levels. Nevertheless, French productivity will probably continue to increase, though at a rate less than that of the past few years.

This belief is based on the knowledge of the substantial amounts of new investment which have been and are being made in postwar France and the progress of French technicians and management in learning American methods of mass production and efficiency. The end of inflation and the restoration of competition which will come from that as well as from the greater liberalization of international trade, should also result in a more efficient utilization of the labor force.

(Despite substantial evidence that French productivity will continue to increase, the basic factors which held prewar industrial productivity in France to one-third that of the U.S. and now keep it nearer one-fourth, are still operating. For a fuller discussion of this problem see "Review of the French Second Annual Program" Paris TOECA/TOREP Despatch 266, December 15, 1949.)

The Dollar Gap

France has made very substantial progress in its balance of payments with the entire world. One dramatic illustration of this was given on May 2, 1950 when France turned back \$21,750,000 of multilateral drawing rights to which she was entitled.

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In the first quarter of 1950 France had a deficit with her partners in the Marshall Plan of only \$11.6 million. This is to be compared with a deficit of \$57.5 million a year earlier. This deficit, or actually the non-dollar deficit, is extremely small. This can be seen by comparing it to France's total production which in 1949 was estimated at over \$20 billion. Furthermore, there is reason to believe that France could run a surplus with the non-dollar world. But even if it does not, the possible deficit will certainly be of "manageable" proportions; one which could be absorbed, if necessary, without any serious readjustment in the French standard of living.

But for France, as for most of the other ERP countries, the dollar problem remains as the persistent hard-core of its external financial difficulties. For France, it is the only balance of payments problem of magnitude.

All the recent estimates of the French dollar balance of payments in 1952/53 show a deficit of between \$150 and \$200 million. Table 1 below contains a summary of the major factors involved.

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Table 1

FRENCH UNION: GOLD AND DOLLAR BALANCE
OF PAYMENTS ESTIMATE, 1952/53
(millions of dollars)

| | | |
|--------------------------------|------------|-------|
| Imports | 285 | |
| Exports | <u>190</u> | |
| Net Trade | | - 95 |
| Freight, net | | 0 |
| Tourism, net | | / 100 |
| Interest and amortization, net | | - 155 |
| OT Balance | | - 25 |
| Net Balance, current account | | - 175 |

Source: ECA/Washington. These estimates are similar to those of French which indicate a deficit of between \$150 and \$165 million.

Note: Prices are average 1949 prices.

Estimating two or three years into the future is obviously an extremely hazardous task. For this reason the focus of our attention should be on the policies which France and the U. S. must follow in order for France to achieve viability rather than on refinements in the estimates.

Dollar imports: - Progress in reducing the dollar deficit thus far has depended almost entirely on a reduction in imports. This was entirely expected. Imports during the early postwar years were swollen by the

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needs of replacing the wartime destruction and poor harvests and the inability of any of France's neighbors, faced with the same problems, to supply the goods which were required.

Between now and 1952/53 further substantial reductions in imports will be required. In 1949/50 France is expected to import about \$490 million of goods from the dollar area. This will have to drop to about \$285 million by 1952/53.

In order to achieve a restriction of this magnitude, controls over the use of dollar exchange will have to be maintained. Further devaluation with respect to the dollar might reduce the stringency of some of these controls but devaluation is not now considered by either the French or the U. S. governments to be necessary or desirable.

When supplemented by imports from other countries and by France's own production, the projected level of dollar imports will be sufficient to support the rising standard of living which is assumed. Table 2 below compares the probable commodity composition of the imports with that programmed for the current fiscal year.

Table 2

METROPOLITAN FRANCE: GOLD AND DOLLAR IMPORTS

(millions of dollars)

| | 1949-50 final program | 1952-53 ECA/W est. |
|--------------------|-----------------------|--------------------|
| Petroleum and | | |
| Petroleum products | 100 | 85 |
| Raw cotton | 101 | 85 |
| Equipment | 154 | 45 |
| Copper | 134 | 25 |
| Other | 489 | 45 |
| Total | 489 | 285 |

Note: Imports under EFAC and 10% equipment allowances are not included.

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As can be seen, the major reduction from 1949/50 is in imports of equipment. The estimate of equipment imports in 1952/53 represents entirely replacement parts for U.S. equipment now in France. France itself will produce a large quantity of the equipment and it will rely on European sources for the remainder. It would be desirable for France to import more dollar equipment but this seems to be economically impossible without increased U.S. private investment and not absolutely necessary. (Note that before the war France imported only minor amounts of U.S. equipment.)

The reduction in dollar petroleum imports from \$100 million in 1949/50 to \$85 million in 1952/53 should not mean any hardship. Petroleum can be readily procured with sterling. Actually one of the means France will probably employ to resolve the dollar deficit would be to reduce even further its dollar payments for petroleum. This could be achieved by shifting even more to purchases of sterling oil, by maintaining a high internal price for petroleum products and therefore reducing the domestic demand for it, and finally by negotiating with the U.S. companies to accept part payment for petroleum in francs.

The reduction planned in dollar cotton imports is no doubt also "manageable" but to date France has made no serious steps to find a replacement for U.S. cotton supplies. This may have serious implications for the French cotton textile industry but its impact on the entire economy should not prove serious.

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Dollar Exports - French exports to the dollar area are expected to increase from \$111 million per annum, achieved during the first nine months of 1949 before the devaluation, to \$190 million in 1952/53. Though this is a substantial increase, percentagewise, it is insignificant when compared to the size of the American market. An aggressive French marketing policy, the establishment of a network of distribution channels in the U.S., plus market research and an advertising campaign, is required, however. Since dollar sales are much more essential to the French economy than they are to the individual French producer who usually has adequate outlets at home or elsewhere in Europe, the responsibility for an aggressive and well organized selling campaign in the U.S. is largely that of the government. The government has unfortunately been slow in rising to the challenge.

Overseas Territories: - The overseas territories will probably run a small net deficit, approximately \$25 million in 1952/53. The earlier optimism the French had shown with regard to a large dollar surplus of the overseas territories by 1952/53 is not justified.

A sharp improvement in the economic situation of the overseas territories by 1952/53 is possible, however. The most important factor would be an early end to the war in Indo-China. This would permit a reduction in the French military effort with a consequent easing of French internal economic pressures and some savings on dollar imports.

Deficit: - As near as can be estimated, the current account dollar deficit in 1952/53 will be around \$175 million. This is actually a "manageable" deficit. A fall in the prices of raw materials which constitute French principal imports from the U. S. could wipe out a part of the deficit.

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An increase in the amount of private U. S. investment in France or in the overseas territories could also account for another part. Finally, if the situation remained difficult, France could no doubt procure from the sterling area most, if not all, of the \$85 million of petroleum imports now planned, or deals with the U. S. petroleum companies whereby the latter accept part payment in francs, could be arranged.

On the basis of the estimates presented in the table ~~mm~~ above, it now seems probable that France will not be able to meet its debt repayment obligations on U. S. loans. The projected repayments on U. S. government loans are given in Table 3, below.

Table 3

FRENCH PAYMENTS ON U. S. GOVERNMENT LOANS

(millions of dollars)

| | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|------|------------------|-----------------|--------------|
| 1950 | 21.7 | 46.6 | 68.3 |
| 1951 | 44.5 | 46.0 | 90.1 |
| 1952 | 69.2 | 47.0 | 116.2 |
| 1953 | 70.0 | 47.4 | 117.4 |
| 1954 | 70.8 | 45.6 | 116.4 |

The amount due to the U. S. government in 1952/53 covers two-thirds of the estimated deficit. Thus it seems advisable that the U. S. work out a way to eliminate or refinance French post-war government debt. Our estimates indicate the action required. The exact type of action which is to be taken is a delicate political question; it would be undesirable for the U. S. to allow France to default.

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